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On Behalf of the Emergency Committee for American Trade

Before the U.S. International Trade Commission
Re: Steel-Consuming Industries: Competitive Conditions with Respect to Steel Safeguard Measures
USITC Inv. No. 332-452

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Madam Chairwoman, Commissioners, Members of the Staff, I'm Dan Murphy Caterpillar's Vice President for Global Purchasing. In that capacity I'm responsible for the $14 billion of goods and services that Caterpillar buys every year from around the world. Within that universe I'm here today to discuss Caterpillar's experience buying more than a billion dollars of raw steel and steel fabrications since the United States imposed steel tariffs in March 2002. I'm also here today representing one of the most respected trade organizations in Washington – the Emergency Committee for American Trade (ECAT).

Together Caterpillar and the other ECAT companies have combined annual sales of nearly $2 trillion, and employ over 5 million people. ECAT member companies – such as Caterpillar, Case New Holland, Emerson, Illinois Tool Works, Deere & Company, and Maytag – are among the best customers of the American steel industry. ECAT companies produce some of America's best-known products – including agriculture and construction equipment, electric motors, tools, household appliances, food processing machinery, and automobiles. And our factories go head-to-head with competitors from around the world. Furthermore, the overwhelming majority of steel purchases by many ECAT companies have traditionally and still come from domestic mills.

As you will recall following the initiation of the original Section 201 investigation, Caterpillar, ECAT and several of the other ECAT member companies actively participated in the ITC's original investigation and with respect to the Administration's decisions on remedies. The guidance we provided can be easily summarized. Given that many of the integrated steel mills faced enormous legacy cost problems, we believed some help to the steel companies was needed. Consequently, we supported President Bush's initiative to eliminate excess, non-economic steel-making capacity throughout the world. We supported a more comprehensive worker adjustment program to provide additional training and a better safety net for displaced workers. We urged the President to use general revenues to promote steel industry consolidation and restructuring in the United States. And we also said that we would not object to some type of Tariff Rate Quota (TRQ) arrangement ... provided the goal was to prevent a future surge of imported steel and the arrangement was consistent with our WTO obligations.

At the same time, Caterpillar and ECAT strenuously opposed suggestions that the United States should impose tariffs on fairly-traded steel. We pointed out that because of Caterpillar's size and sophistication, we could likely manage the negative consequences of tariffs and quotas better than other U.S. manufacturers; however, we knew that a quick-fix solution based on high import tariffs could devastate many of our smaller suppliers in our supply chain. Furthermore, we believed that because steel imports were declining for several years prior to the 201 investigation, the imposition of high import tariffs at that point would likely violate America's WTO obligations.

It has now been 15 months since the imposition of safeguard tariffs. During that time ECAT companies have seen – as they expected – significant detrimental effects as a result of the President's imposition of safeguard tariffs, including:

- Higher prices: The double whammy of having domestic capacity lowered as a result of bankruptcies and prohibitively high tariffs effectively reduced supply in the U.S. market and contributed swiftly to significant price increases on the spot market ... forcing some to renegotiate long-term contracts. ECAT members experienced price increases for different products of as much as 45 percent or even higher for certain products throughout the summer until demand leveled somewhat.

- Lack of availability of key products: Several ECAT companies experienced significant problems in obtaining key products. Supplies of many key grade and gauge combinations became difficult to obtain from U.S. producers, even under the clear terms of written supply agreements. Just-in-time delivery was undermined or used as leverage by the domestic steel industry to obtain price increases. Delays in receiving needed inputs undermined the competitiveness and reliability of some of America's steel-intensive industries.

- Trade retaliation: As we expected, the World Trade Organization has already issued an interim ruling that the steel tariffs are out of compliance with America's trade obligations. As a result, after WTO appeals are exhausted this autumn, the EU and others may be in a position to impose retaliatory tariffs that will further hurt the U.S. and world economies.

It wasn't easy, but Caterpillar was able to mitigate some of the negative impacts of the steel 201 tariffs. During the section 201 investigations, we realized that unless the company moved quickly our steel prices could increase by at least 30 percent. As a result, Caterpillar immediately initiated several 6 Sigma project teams to investigate our global steel purchasing needs in light of the anticipated restrictions on steel supplies. These teams developed data that enabled new successful negotiating strategies. Caterpillar expanded its list of approved suppliers and created increased competition among these suppliers for certain products. Caterpillar found cost-savings for its steel fabricators as well. While not accepting price increases from its steel fabricators, Caterpillar increased by 57 percent its raw steel supplies to fabricators through our "steel-to-fabricator" program. Another 6 Sigma team looked at ways to make sure the Commerce Department had all the information it needed to evaluate the merits of Caterpillar's steel import exclusion requests.

Unfortunately, even with these actions, Caterpillar did not fully escape the negative impact of the steel tariffs. While an expansion of the steel-to-fabricator program helped, many suppliers - some that are family-owned - have not been able to manage during these tough times. Overall the bankruptcy and high-risk notification rate of our suppliers, many producing steel intensive products, climbed 22 percent in the last 18 months. When steel suppliers were not able to meet their contractual obligations, Caterpillar was forced to go to the high-priced spot market to meet certain raw steel needs. Caterpillar took a 40-to-50 percent cost increase on the spot market for hundreds of tons during June and July 2002. Furthermore, during the second half of 2002, Caterpillar's purchases of forging bars and hot-rolled alloy and carbon bars from domestic producers were routinely hampered by long lead times. In fact, during late 2002, one producer increased lead times that typically averaged 5 to 8 **weeks** to 5 to 6 **months**. This trend improved marginally by April and May of 2003, but lead times still average 3 to 4 months, or roughly double the norm.

Finally, Caterpillar and the Commerce Department did not see eye-to-eye on excluding tariffs on products where there is only one domestic source. Commerce was not sympathetic to our argument that in such cases the tariff provides near monopoly pricing power … and as a result contributes to sharply higher prices. To add insult to injury all these actions required us to expend considerable management resources reacting to the tariff measures that could have been devoted to improving the long-term competitiveness of our U.S. manufacturing operations.

Other ECAT companies have similar stories: they have faced higher prices and limited supply and longer lead times. For some, the only competitive option left was to shift some production to facilities located outside the United States that do not restrict the supply of steel.

So where are we today? We can argue over the degree, but as a general rule it is fair to say that steel tariffs have hurt America's steel-using manufacturers, especially the small family-owned companies that buy steel on the spot market. As a result, the steel tariffs have hurt the overall economy and compromised America's leadership position in global trade negotiations.

While we recognize that steel prices have moderated and that steel supply has loosened up since 2002, it is important for the Commission to put those conditions in the wider context of U.S. economic conditions. These are not easy times. American manufacturing and agriculture are in the midst of a prolonged economic downturn. Sales are flat, even at leading U.S. companies. America's consumers are worried. Since July 2000, more than 2 million U.S. manufacturing jobs have disappeared. The number of U.S. manufacturing jobs has fallen for 33 consecutive months. The European and Japanese economies are also struggling and may require long-term structural reforms. As a result, overseas demand for U.S. products is likely to be uncertain for some time. Even the best U.S. companies face intensifying global competition and the looming threat of price deflation in some overseas markets.

These overall conditions obviously have affected the U.S. steel market, helping to lower steel prices, as demand for steel is reduced and domestic steel availability increases. This should not, however, lead one to conclude that the safeguard tariffs have not been and, if continued, will not continue to be costly to domestic steel users. Indeed, the continued imposition of substantial tariffs puts U.S. manufacturing companies at a disadvantage globally and undermines the prospects for robust growth in the U.S. economy. If, as we all hope, the U.S. market reverses course and experiences strong economic growth, we expect that demand for steel in the U.S. market will increase. As a result of artificially-reduced supply caused by the prohibitively high tariffs, domestic steel prices can be expected to increase substantially again and availability will continue to be restricted. These factors, in turn, will limit the competitiveness of U.S. steel purchasers, who, as a result of price and availability concerns, will be less able to enjoy the benefits or promote a sustained U.S. recovery. Continuing to undermine the competitiveness of American steel using manufacturers will therefore hurt, not help, the very steel industry that the safeguard action was intended to benefit.

From the perspective of Caterpillar and ECAT, the bottom line is this: a sustained U.S. economic recovery requires a healthy American manufacturing sector, and a healthy American manufacturing sector requires a timely end to steel safeguard tariffs. While eliminating the tariffs will not solve the macroeconomic problems of slow economic growth and lower demand, it will enable U.S. companies to once again position themselves as reliable and cost-competitive suppliers, enabling them to compete on a more equal footing in the international marketplace.

Increasingly, the question is, where do we go from here. As I mentioned earlier, prior to the imposition of the safeguard tariffs, Caterpillar and ECAT argued that there were actions that the United States could take to help the steel industry. We still believe that some of those remedies are appropriate.

The American steel industry is <u>not</u> alone in facing global competition. In the 1980s, ECAT and other U.S. companies worked hard to meet the challenges of a global economy in economic decline. Today, the United States is again recognized as a global leader in manufacturing, finance, agriculture, and services because American companies met these challenges by embracing competition, innovation, open trade and globalization.

It is time to move on. It is time for our government to adopt policies that will enhance the global competitiveness of the entire U.S. manufacturing sector. It is time for our government to adopt policies that promote economic efficiency by improving competitiveness at home and opening foreign markets. It is time for our government to find another way. It is time to end tariffs on fairly-traded steel.

Thank you.